

What's New and Other Important Information for 2004

Amnesty – Recent legislation authorizes the Franchise Tax Board and the Board of Equalization to administer a Tax Amnesty Program. Tax amnesty is a limited time chance for individuals and businesses to pay past-due income, franchise, sales, or use taxes and the related interest penalty-free without the fear of criminal prosecution. Amnesty runs from February 1, 2005, through March 31, 2005. Taxpayers eligible to participate in amnesty but choose not to do so will be subject to additional penalties.

Amnesty is open to both individuals and businesses for taxable years 2002 and prior, if they did any of the following:

- Did not file required California tax returns.
- Underreported income on a previously filed tax return.
- Claimed excessive deductions.
- Did not pay income/franchise, sales, or use taxes on time.

The following taxpayers or transactions are not eligible for amnesty:

- Taxpayers currently under criminal investigation or prosecution on tax-related matters.
- Abusive tax shelter transactions that were eligible for relief under California's Voluntary Compliance Initiative or the 2003 IRS Offshore Voluntary Compliance Initiative. These initiatives applied to taxpayers with nonreported or underreported tax liability amounts attributable to an investment in an abusive tax shelter.

Note: These taxpayers are eligible for amnesty for non-abusive tax shelters items.

For more details, visit our Website at www.ftb.ca.gov or call (800) 852-5711.

Tax Shelters – If you were involved in a potentially abusive tax shelter, you may have a disclosure, registration, and list maintenance requirement. The Franchise Tax Board may impose several new and enhanced penalties if you fail to file IRS Forms 8886, 8264, 8271 or any required information. For more information, see Registration and Reporting Requirements under Abusive Tax Shelters on our Website at www.ftb.ca.gov.

Differences between California and Federal Law

In general, California law conforms to the Internal Revenue Code (IRC) as of January 2001. However, there are continuing differences between California and federal law. When California conforms to federal tax law changes, we do not always adopt all of the changes made at the federal level. For more information regarding California and federal law, please visit our Website at www.ftb.ca.gov and select "Law and Legislation." Additional information can be found in FTB Pub. 1001, Supplemental Guidelines to California Adjustments, the instructions for California Schedule CA (540 or 540NR), and the Business Entity tax booklets.

Note, the instructions provided with California tax forms are a summary of California tax law and are only intended to aid taxpayers in preparing their state income tax returns. We include information that is most useful to the greatest number of taxpayers in the limited space available. It is not possible to include all requirements of the California Revenue and Taxation

Code (R&TC) in the tax booklets. Taxpayers should not consider the tax booklets as authoritative law.

2004 Tax Law Changes

Federal Conformity Items – California has conformed to the Military Family Tax Relief Act (Public Law 108-121) to allow the following:

- A deduction in computing adjusted gross income for certain trade or business expenses of members of the Armed Forces of the U.S.
- An exclusion from gross income for certain death benefits payable by reason of the death of astronauts
- An exclusion for certain military fringe benefits
- A 5-year period of suspension for excluding gain from the sale of a principal residence if the taxpayer's spouse is serving in the uniformed services or the Foreign Service of the U.S.
- An exclusion for certain military death gratuity payments from gross income
- An exclusion for death gratuity income received by living survivors of military personnel who lost their lives on or after September 11, 2001.

Military Personnel – Servicemembers domiciled outside of California, and their spouses, may exclude the member's military compensation from gross income when computing the tax rate on nonmilitary income. Requirements for military servicemembers domiciled in California remain unchanged. Military servicemembers domiciled in California must include their military pay in total income. In addition, they must include their military pay in California source income when stationed in California. However, military pay is not California source income when a servicemember is permanently stationed outside of California. For more information, get FTB Pub. 1032, Tax Information for Military Personnel.

Alimony Deduction – If you were a nonresident of California in 2004, you are now entitled to an alimony deduction. The deduction for alimony payments is allowed to a nonresident or part-year resident in the same ratio that "California AGI" for the entire year, computed without regard to the alimony deduction, is to "Total AGI" for the entire year, computed without regard to the alimony deduction.

Changes in the Child and Dependent Care Expenses Credit:

- Earned income must have a source in California
- Dependent Care must be provided in California

Paid Family Leave Benefits – If you received paid family leave benefits in 2004, they are not taxable by California. For additional information, get Schedule CA (540NR) and instructions – California Adjustments, and get FTB Pub. 1001 – Supplemental Guidelines to California Adjustments.

Claim of Right – If you had to repay an amount that you included in income in an earlier year, under a claim of right, you may be able to deduct the amount repaid from your income for the year in which you repaid it. Or, if the amount you repaid is more than \$3,000, you may be able to take a credit against your tax for the year in which you repaid it.

Punitive Damage Awards – For court actions filed after August 16, 2004, and finally adjudicated by June 30, 2006, 75% of punitive damage awards must be paid to the Director of the Department of Finance. You may exclude from income the portion

of a punitive damage award that is paid to the Department of Finance.

Other Important Information

San Joaquin Levee Break – If you were a victim of the San Joaquin levee break, get FTB Pub. 1034, California Disaster Relief Tax Provisions and Pub. 1034A-6, San Joaquin Levee Break, for more information.

Mandatory e-file – California law requires individual income tax returns prepared by certain tax practitioners to be e-filed. This law saves money and resources for the state. If you have a tax practitioner prepare your return, they may be required to e-file it. You have the right to choose not to e-file, however, we encourage you to take advantage of everything e-file has to offer.

Vehicle License Fee (VLF) Refund – If you paid a VLF and deducted the fee as an itemized deduction for 2003, the VLF refund you received in 2004 is treated as a recovery of the amount you claimed as an itemized deduction. For more information, get Schedule CA 540NR and instructions – California Adjustments – Nonresidents or Part-Year Residents, and FTB Pub. 1001, Supplemental Guidelines for California Adjustments.

Teacher Retention Credit – The Teacher Retention Credit is suspended for tax years 2004 and 2005.

Net Operating Loss – For taxable years beginning on or after January 1, 2004, California has reinstated the Net Operating Loss (NOL) carryover deduction. The carryover periods for NOL deductions that were incurred:

- Beginning before January 1, 2002, has been extended for two years.
- Beginning on or after January 1, 2002, and before January 1, 2003, has been extended for one year.

Natural Heritage Preservation Credit – Currently there is no funding to award Natural Heritage Preservation Credits. Therefore, no new credits may be claimed for 2004. However, carryover of previously awarded credits is not affected. Contact the Wildlife Conservation Board (WCB) to determine if funding has been restored, if they are accepting qualified contributions of property, and to see if they are awarding new Natural Heritage Preservation Credits. Complete form FTB 3503 to claim the credit only if the WCB has resumed awarding the credits.

To get updated information regarding current funding, qualified contributions of property, or the awarding of credits, contact the Wildlife Conservation Board at (916) 445-8448. Or go to their Website at www.wcb.ca.gov.

New Voluntary Contribution Funds – You may make voluntary contributions to the California Military Family Relief Fund and/or the California Prostate Cancer Research Fund.

NO MORE TELEFILE!

TeleFile – TeleFile is no longer available to file California tax returns. We discontinued TeleFile due to decreasing usage and to help save California resources. If you qualified for TeleFile, you also qualify to use our free e-file option: CalFile. Like TeleFile, CalFile is fast, direct, and easy to use. Go to www.ftb.ca.gov to use CalFile or other free options available online including California e-file options and the Federal Free File Alliance.